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Petition of Cambridge Electric Light Company and Commonwealth Electric Company for Approvals Relating to the Termination of Purchase Power Agreements with Pittsfield Generating Company, L.P.

APPEARANCES:

Robert N. Werlin, Esq.
John K. Habib, Esq.
Keegan, Werlin & Pabian, LLP
265 Franklin Street
Boston, MA 02110
FOR: CAMBRIDGE ELECTRIC LIGHT COMPANY/
COMMONWEALTH ELECTRIC COMPANY
Petitioners

Thomas F. Reilly, Attorney General
By: Colleen McConnell
Wilner Borgella, Jr.
Joseph W. Rogers
Assistant Attorneys General
One Ashburton Place
Boston, MA 02108
Intervenor

John A. DeTore, Esq.
Rebecca L. Tepper, Esq.
Rubin and Rudman LLP
50 Rowes Wharf
Boston, MA 02110
FOR: PITTSFIELD GENERATING COMPANY, L.P.
Intervenor

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I. INTRODUCTION

On June 29, 2004, pursuant to G.L. c. 164, §§ 1A, 1G, 76, 94, and 94A, Cambridge Electric Light Company ("Cambridge") and Commonwealth Electric Company ("Commonwealth") d/b/a NSTAR Electric (jointly "the Companies" or "NSTAR Electric"), filed with the Department of Telecommunications and Energy ("Department") for approval of two termination agreements with Pittsfield Generating Company, L.P. ("Pittsfield") ("Termination Agreements"), and approval of ratemaking treatment relating to the Termination Agreements. The Termination Agreements terminate a 1992 purchase power agreement ("PPA") between Cambridge and Pittsfield, and a 1992 PPA between Commonwealth and Pittsfield. Under those 1992 PPAs, as amended, Cambridge and Commonwealth each are required to pay for the delivered energy and capacity for 17.2 percent of the output of Pittsfield's electric generating plant through December 31, 2001 (Exhs. NSTAR-GOL at 12; NSTAR-CAM-GOL-1; NSTAR-COM-GOL-1). The Department docketed this matter as D.T.E. 04-60.

II. PROCEDURAL HISTORY

Pursuant to notice duly issued, the Department conducted a public hearing and procedural conference on July 21, 2004. The Attorney General of the Commonwealth of Massachusetts ("Attorney General") filed a notice of intervention as of right pursuant to G.L. c. 12, § 11E. The Department granted full intervenor status to Pittsfield. The Department conducted an evidentiary hearing on August 5, 2004. The Companies sponsored the testimony of Geoffrey O. Lubbock, vice president, financial strategic planning and policy for NSTAR Electric and Gas Company, and Robert B. Hevert, president of Concentric Energy Advisors, Inc. ("CEA"). The Companies, the

Attorney General, and Pittsfield filed initial briefs on August 12, 2004, and reply briefs on August 17, 2004. The evidentiary record includes 132 exhibits and the Companies' responses to twelve record requests.

III. ATTORNEY GENERAL'S MOTION TO STRIKE

On August 17, 2004, the Attorney General filed a Motion to Strike Portions of the Initial Brief of Pittsfield Generating Company ("Motion"). On August 20, 2004, Pittsfield filed its Reply to the Motion ("Reply").

In its Motion, the Attorney General asserts that during the evidentiary hearing on August 5, 2004, the Hearing Officer made a ruling from the bench that limited the scope of the proceedings, and that portions of Pittsfield's initial brief contain arguments regarding the issues the Hearing Officer explicitly excluded from consideration in the proceeding (Motion at 1). The Attorney General contends that he was prejudiced when Pittsfield addressed issues on brief that the Attorney General was barred from exploring during cross-examination by the Hearing Officer's ruling (id.). The Attorney General identifies portions of Pittsfield's brief to be stricken that address a dispute between the Companies and Pittsfield regarding the existing PPAs,[1]

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[1] The Companies stated that as of September 2003, Pittsfield modified its practices and began selling natural gas when that provided a higher return than sales of energy to NSTAR Electric (Exh. AG- 1-10). According to the Companies, at that time Pittsfield also began offering its electrical output to the New England market at increasing price offer blocks based on spot gas (Exh. AG-2-8). The Companies stated that this modification resulted in significantly reduced dispatch of Pittsfield (Exh. AG-2-1). The Companies noted that this modification coincided with Pittsfield's loss of US Gen New England as an entitlement holder due to its bankruptcy (Exh. AG-2-8). The Companies stated that this modification is the subject of a dispute as Pittsfield believes that this new practice is within its contractual rights, while NSTAR Electric believes that this new

(continued…)

including interpretations of the parties' rights and obligations under the existing PPAs, the parties' level of compliance with the terms of the PPAs, and references to extra-record documents (id. at 2-4). According to the Attorney General, the Department should strike the portions of Pittsfield's initial brief that are outside the scope of the proceeding (id. at 4).

Pittsfield argues that it was the Attorney General that introduced the issue of the PPA contract interpretation into this proceeding, and therefore his attempt to exclude opposing legal arguments should be rejected (Reply at 1). Pittsfield contends that if the Department were to exclude from the scope of this proceeding all issues relating to the interpretation of the PPAs, then most of the Attorney General's initial and reply briefs would also fall outside the scope of the proceeding and must also be struck because the briefs deal extensively with interpretation of the PPAs (id. at 2-3). Pittsfield points to multiple portions of the Attorney General's briefs that address the dispute between the Companies and Pittsfield, and the Companies' possible avenues of recourse under the PPAs (id.).

Pittsfield also argues that the Hearing Officer did not exclude from the scope of this proceeding issues related to interpretation of the PPAs or to prohibit the parties from making legal argument regarding the PPAs on brief (id. at 5). Pittsfield provides the context in which the ruling was made, and concludes that the Hearing Officer was responding to Pittsfield's concern that it would be prejudiced by being excluded from a closed session; the Hearing Officer ruled that Pittsfield would not be prejudiced by being excluded because the witnesses would not be

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[1](…continued)
practice is inconsistent with the contract's intent (Exh. AG-1-10).

providing testimony regarding contract interpretation (id. at 6). Pittsfield points out that the witnesses to be questioned during the closed session are not attorneys, and therefore were properly prohibited by the Hearing Officer from testifying on interpretation of the PPAs (id.). Pittsfield argues that issues of PPA contract interpretation were not excluded by the Hearing Officer, but were to be addressed on brief (id. at 8).[2] Finally, Pittsfield argues that two documents[3] that the Attorney General classifies as extra-record have been filed with the Department or are incorporated into regulatory proceedings of the Department, and that the Department may incorporate by reference or take official notice of the documents (id. at 10-11).

The Hearing Officer's ruling must be taken in the context in which it was given; the question before the Hearing Officer was whether Pittsfield would be prejudiced by being excluded from the closed session (Tr. at 187-195). The Attorney General sought to question the Companies' witnesses on two emails that discussed certain pricing information regarding the Pittsfield plants (id. at 187). The Companies argued that Pittsfield should be excluded from the closed session because the emails disclosed internal discussions on the dispute and the potential value of the contracts (id. at 188-189). Pittsfield argued that it would be prejudiced by being excluded, because of a concern that in closed session the Attorney General would pursue evidence

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[2] Pittsfield contends that because no party was allowed to cross-examine the witnesses regarding contract interpretation, the Attorney General stands in no different position than Pittsfield and the Companies, and therefore suffered no prejudice as a result of the Hearing Officer's ruling (Reply at 10).

[3] The documents are the New England Power Pool ("NEPOOL") Agreement, and an attachment to the PPAs that was filed with the Department with the original PPAs (Reply at 10-11).

on certain interpretations of the PPAs that would be potentially detrimental to Pittsfield's interests (id. at 190).

The Hearing Officer ruled that Pittsfield would not be so prejudiced (id. at 194-195). First, the Hearing Officer determined that the cross-examination during the closed session would not center on interpretations of the PPAs, because the witnesses were not lawyers and therefore not competent to testify on contract interpretation (id.). Accordingly, the Hearing Officer ruled that the non-lawyer witnesses could not be cross-examined on contract interpretation during the closed session (id.). Second, the Hearing Officer ruled that the instant proceeding would not determine whether Pittsfield had breached the PPAs, because this is not a proceeding on interpretation of the existing PPAs (id.). Even if the Department were the proper forum for a determination of whether Pittsfield's dispatch actions are consistent with the PPAs, there is not a sufficient record here to make that decision. Determination of whether Pittsfield breached the PPAs is outside the scope of this proceeding.

The briefs of Pittsfield and the Attorney General both contain legal argument on the interpretation of what the Companies and Pittsfield may do legally under the PPAs. To the extent that they ask the Department to make a determination on what the PPAs require or allow, such argument is outside the scope of this proceeding. However, based on our decision below, it is unnecessary to strike any portions of Pittsfield's briefs as the Attorney General has requested, because the Department did not use Pittsfield's arguments on which to base a decision on the Termination Agreements before us. The Attorney General suffered no prejudice from the

arguments included in the Pittsfield briefs. Therefore, the Department denies the Motion of the Attorney General.

IV. STANDARD OF REVIEW

An electric company that seeks to recover transition costs must take efforts to mitigate those costs to the maximum extent possible. G.L. c. 164, §§ 1G(d)(1) and (2). As part of its mitigation efforts, the company must make a good faith effort to renegotiate any above-market power purchase contracts. Id. If a negotiated contract buyout or other modification to the terms and conditions of such contracts is likely to achieve savings to the ratepayers and is otherwise in the public interest, the Department may allow the company to recover the remaining amounts in excess of market value associated with the contract in the transition charge. G.L. c. 164, §§ 1G(b)(1)(iv) and 1G(d)(2).

In determining whether to approve a power contract buyout, buy-down, or renegotiation, the Department has applied its standard of review for settlement agreements, i.e., a standard of reasonableness. See e.g., Canal Electric Company/Cambridge Electric Light Company/Commonwealth Electric Company, D.T.E. 02-34, at 21 (2002); Cambridge Electric Light Company, D.T.E. 01-94, at 7 (2002); Commonwealth Electric Company, D.T.E. 99-69, at 7 (1999); Boston Edison Company, D.T.E. 99-16, at 5-6 (1999); Western Massachusetts Electric Company, D.T.E. 99-56, at 7-8 (1999). The Department must review all available information to ensure that the agreement is in the public interest. See, e.g., Western Massachusetts Electric Company, D.T.E. 99-101, at 5-6 (2000); Commonwealth Electric Company, D.P.U. 91-200, at 5 (1993). In determining whether a contract amendment or termination is consistent with the public

interest, the Department has considered whether the termination is consistent with a company's approved restructuring plan. In Cambridge Electric Light Company/Commonwealth Electric Company/Canal Electric Company, D.P.U./D.T.E. 97-111, at 90 (1998), the Department found that Cambridge and Commonwealth's restructuring plan, which provided for the buyout of above-market purchase power obligations, was consistent or substantially complied with the Restructuring Act (the "Act")[4].

V. THE AUCTION PROCESS AND TERMINATION AGREEMENTS

A. Overview

NSTAR Electric proposes the buyout and termination of Cambridge's and Commonwealth's respective PPAs with Pittsfield. Under these PPAs, Cambridge and Commonwealth are each entitled to 17.2 percent of the output of a generation facility in Pittsfield, Massachusetts[5] (Exh. NSTAR-RBH at 24). Each PPA includes payments for energy and capacity, and the Cambridge PPA also includes a transmission charge (id.). Both PPAs are to terminate on December 31, 2011 (id.). The Companies propose to terminate the PPAs as the result of a PPA divestiture plan ("auction") initiated by the Companies in July 2003 (Exh. NSTAR-RBH at 5).

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4 St. 1997, c. 164.

5 Pittsfield is a gas-burning combined-cycle cogenerating facility located in Pittsfield, Massachusetts, formerly known as Altresco Pittsfield, L.P. (Exh. NSTAR-GOL at 12). The plant's current summer and winter capacity ratings are 141 MW and 173 MW, respectively (id.).

B. The Auction Process

At the outset of the auction, the Companies identified four primary objectives of its divestiture plan: (1) minimize the above-market costs associated with the PPA entitlements; (2) develop, implement, and maintain the most competitive auction process possible; (3) ensure fair treatment of all bidders; and (4) ensure that the auction process was timely, efficient, and unbiased (Exh. NSTAR-RBH at 5). Under this plan, 24 separate PPAs were contemplated for sale or transfer (Exh. NSTAR-RBH at 4). CEA was selected to assist in the divestiture of these PPAs (Exhs. NSTAR-1, at 4; AG-1-3; AG-1-3(b); AG-3-2).

The initial marketing phase began on October 1, 2003 when the Companies publicly announced their intention to sell or transfer 24 PPA entitlements (Exh. NSTAR-RBH at 10). Following that announcement, an early interest package ("EIP") was sent to approximately 90 potential bidders (id.). Recipients included counterparties to the PPA entitlements, global, national and regional energy companies, unregulated affiliates of electric and gas utility companies, project developers, energy marketers, financial advisors and investment firms (id.). The EIP included an early interest letter, a confidentiality agreement, and a request for qualifications (id. at 10; Exh. NSTAR-RBH-3). Those bidders who executed a confidentiality agreement were admitted into the auction process (Exh. NSTAR-RBH at 11). The prospective bidders were also required to submit a completed qualification package in order to be considered "Qualified Bidders" (id.). Between October 1, 2003 and November 15, 2003, the Companies

and CEA received responses from 25 interested parties. Subsequently, all 25 prospective bidders completed qualification packages and became Qualified Bidders[6] (id.).

The due diligence stage of the auction process began on October 17, 2003, when an offering memorandum ("OM") was sent to each Qualified Bidder (id. at 13).[7] In addition, the Qualified Bidders received a CD-ROM that included all of the PPA entitlement agreements, amendments, associated invoices, and an evaluation spreadsheet for each of the PPA entitlements (id. at 14). The Companies stated that the due diligence process was designed to ensure that each Qualified Bidder received complete and timely information with respect to contract evaluation (Exh. NSTAR-RBH at 8; Tr. at 127). To that end, each Qualified Bidder was assigned a specific CEA staff member who was responsible for answering the bidder's questions, and if needed, to arrange for meetings or conference calls with the Companies' personnel (Exh. NSTAR-RBH at 8-9). The Companies stated that three Qualified Bidders voluntarily withdrew shortly after receipt of the OM.

On November 6, 2003, bid instructions and a bid form were made available to all bidders (id. at 15). The bid form included two pricing options: (1) a lump-sum payment from the bidder to NSTAR Electric or from NSTAR Electric to the bidder; and (2) energy only pricing, i.e., the

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6 The Qualification Package was designed to provide the Companies and CEA with specific financial, legal, and operating information about the prospective bidders to ensure that all bidders selected for participation in the process had financial and operational capability to assume and administer the PPA entitlements (Exh. NSTAR-RBH at 12). Those selected prospective bidders were given the title "Qualified Bidder" (id. at 11).

7 The OM included a detailed description of the PPA entitlements, an overview of the bidding process, and preliminary terms of sale (Exh. NSTAR-RBH at 14).

price per megawatthour a bidder would pay to NSTAR Electric for energy delivered under the specific PPA entitlement (id.; Exh. NSTAR-RBH-4).

On December 3, 2003, the Companies and CEA received twelve bids; three of those were portfolio bids while nine were contract-specific (Exh. NSTAR-RBH at 17). The Companies and CEA evaluated the bids from December of 2003 through March of 2004 (id.). The process of evaluation included negotiations with the bidders regarding specific aspects of their proposed financial and contractual terms with the objective of identifying those combinations of bids that offered the greatest mitigation of transition costs (id.). Based on these activities, certain bidders were invited to participate in meetings and/or conference calls with the Companies (id.). During those discussions, bidders were provided an opportunity to further clarify and enhance their bids, and various bidders made specific improvements to their bids (id.).

Prior to the bid deadline, the Companies and CEA had developed a bid evaluation method (id. at 18). That method was designed to first estimate the above-market cost of each contract, and then to identify the bid or bids that offered the greatest cost reduction (id.). Accordingly, CEA modeled each contract to project its cost of energy and capacity over the contract term (id.). The cost of an equivalent amount of market-priced energy and capacity was projected using forecast data obtained from Henwood Energy Service Inc. ("Henwood forecast") (id.). The above-market costs were then calculated as the difference between the present value of the expected cost of the contract and the present value of the cost of an equivalent level of capacity and energy based on Henwood information (id.). The Companies stated that when bids were

compared under this method, Pittsfield's bid was identified as most likely to create the greatest reduction in above-market costs (id. at 21-22).

C. The Termination Agreements

The Termination Agreements that are the result of the 2003 auction relieve the Companies of their obligations to purchase or accept electricity produced at the Pittsfield generation facility, and Pittsfield will no longer have an obligation to sell electricity to the Companies (Exh. NSTAR-GOL at 12). Under the Termination Agreements, the Companies together would be required to make $1.67 million in termination payments on a monthly basis to Pittsfield through December 1, 2008 (id.). The Companies state that the Termination Agreements will result in approximately $7 million of ratepayer savings on a net present value basis when compared to the present value of retaining the PPAs (Exh. DTE-2-1; Tr. at 13).

VI. POSITION OF THE PARTIES

A. Attorney General

The Attorney General states that the Department should reject the Companies' petition because they have failed to establish that the proposed Termination Agreements comply with the maximum mitigation requirements of G.L. c. 164, § 1G(d)(1) (Attorney General Brief at 4). The Attorney General notes that, depending on which set of assumptions are relied upon, the customer savings that are likely to result from these Termination Agreements are very small (id. at 4-5).

The Attorney General claims that the Companies failed to explore other ways to terminate the Pittsfield PPAs that may have yielded greater savings to ratepayers (id. at 5). In support of his claim, the Attorney General refers to the dispute between NSTAR Electric and Pittsfield about

the way the power plant has been dispatched since September 2003 (id.). The Attorney General points to the fact that prior to September 2003, the Pittsfield generating unit was a fully contracted unit: the Companies' entitlement in the plant was approximately 35 percent, and USGen New England's entitlement was 65 percent (id. at 6). The Attorney General further notes that in August 2003, USGen New England declared bankruptcy, and its contract with Pittsfield was terminated by the U.S. Bankruptcy Court, resulting in 65 percent of the Pittsfield capacity and output energy becoming uncommitted (id.). Termination of the USGen New England contract coincided with the significant decline in electricity output from the Pittsfield generating unit (id.).

The Attorney General argues that in accordance with the existing PPAs, the Companies pay a significant amount in fixed charges, and as such do not vary with the level of electricity the Pittsfield plant generates (id.). Therefore, the Attorney General concludes that the dramatic reduction in the electricity generated by the Pittsfield plant after September 2003 detrimentally affected the costs payed by the Companies' customers (id. at 5-6). The Attorney General claims that the Companies contacted Pittsfield regarding the decreased output of the plant only on January 26, 2004, four months after the output reduction began, and took no further action to protect their customers from financial harm (id. at 6).

The Attorney General asserts that there is no evidence that NSTAR Electric intervened in the USGen New England bankruptcy proceedings to protect the financial interests of their customers that might have been affected by the termination of the USGen New England contract with Pittsfield (id.). The Attorney General further claims that the Companies did not inform the

Department about the issue of the Pittsfield plant's output reduction and about the effect of such a reduction on the ratepayers' costs (id.). The Attorney General argues that the Companies did not seek an advisory opinion from the Department in these matters (id.). In addition, the Attorney General claims that the Department has jurisdiction to determine issues in a contract dispute (id. n.5, citing Tenaska Mass, Inc., D.P.U. 91-200 (1993) ("Tenaska")).

The Attorney General maintains that the PPA contracts specify the Companies' right to dispatch the Pittsfield unit (id. at 7). The Attorney General further notes that the Companies did not explicitly request, as the could have under the terms of the contract, that the Pittsfield plant be dispatched at the more economic higher output levels (id.). Instead, the Companies provided only a single letter to Pittsfield indicating that the Companies were dissatisfied with the recent performance of the unit (id. at 7). The Attorney General concludes that the Companies failed to exercise their full contract rights to settle disputed matters (id. at 5). The Attorney General states that the termination of Pittsfield PPAs for nonperformance could have saved customers up to $95 million based on CEA's above-market cost assumptions (id. at 9).

The Attorney General argues that the Companies and CEA did not adequately evaluate several factors to determine the value of the Pittsfield PPAs, such as the termination of USGen New England's PPA with Pittsfield and NSTAR Electric's dispute with Pittsfield (id.). The Attorney General disagrees with the Companies' assertion that CEA only factored into the valuation of the Pittsfield PPAs the decline in the Pittsfield plant's output, not the dispute itself, and was not familiar enough with the terms of the dispute to offer any option on how the Companies should resolve it (id. at 10). The Attorney General argues that had the Companies

examined their options under the Pittsfield PPAs more closely, they may have been able to negotiate a better termination agreement with Pittsfield, or simply terminate the Pittsfield PPAs unilaterally based on Pittsfield's nonperformance (id. at 8). Therefore, the Attorney General suggests the Department should not approve the petition without an appropriate assessment of the value of the Pittsfield PPAs (id. at 10).

The Attorney General states that the Department should disregard Pittsfield's arguments regarding contract breach and Pittsfield's legal interpretation of the parties rights under the existing contracts (Attorney General Reply Brief at 2-4). According to the Attorney General, Pittsfield's argument suggests that NSTAR Electric negotiated PPAs that would cost customers over $24 million a year without the promise of delivering a single kilowatthour (id. at 5, citing Exhs. NSTAR-CAM-GOL-1 and NSTAR-COM-GOL-1). The Attorney General claims that Pittsfield's argument that the Companies do not have the right under the existing contracts to dispatch the unit is supported only by the reference in the contract that "…the Unit will be subject to Economic Dispatch at the sole direction of NEPOOL…" (id. at 5-6, citing Exhs. NSTAR-CAM-GOL-1; NSTAR-COM-1, Article 4.1). But, according to the Attorney General, NEPOOL no longer dispatches generating unit, that ISO New England Inc.("ISO-NE") does (id.). Accordingly, the Attorney General suggests that the Department should disregard Pittsfield's assertion that under the existing contracts only NEPOOL, and not the Companies, may dispatch the unit (id.).

Finally, the Attorney General asserts that a number of calculation errors discovered in the Companies' originally-filed exhibits suggest that there may be other errors that were not

identified during the discovery period (id. at 10). On these grounds, the Attorney General challenges the accuracy of the Companies' models on which the Companies base their filing (id.). The Attorney General argues that the Department should not approve the Companies' petition until the Companies' calculations are independently verified (id. at 10-11). In sum, the Attorney General maintains that the Department should reject the Companies' petition (id. at 11).

B. Pittsfield

Pittsfield requests that the Department grant the petition of NSTAR Electric and approve the Termination Agreements (Pittsfield Brief at 29). Pittsfield states that the PPAs do not require it to meet any specific capacity factor and instead require bids and operation in compliance with current NEPOOL rules and procedures because: (1) no provision of the 1992 PPAs requires that the Pittsfield unit be dispatched at a specific level; (2) the 1992 PPAs contemplated that the Pittsfield unit will be dispatched in accordance with current NEPOOL rules and regulations; (3) current NEPOOL rules and ISO-NE bidding requirements authorize and encourage the inclusion of the full opportunity cost of gas in bids to the ISO-NE; (4) the 1996 amendment to PPAs does not require Pittsfield to obtain approval from the Companies before selling fuel; (5) no provision of the 1992 PPAs allows the Companies to dictate how or when the Pittsfield unit will be dispatched; and (6) the 1992 PPAs are valid contracts that cannot be amended or terminated absent an agreement of the parties (Pittsfield Brief at 9-25). Further, Pittsfield states that the recent operating history of the Pittsfield unit demonstrates that a 37 percent capacity factor is a conservative assumption and that a 90 percent capacity factor for calculating the savings associated with the Termination Agreements is inappropriate (id. at 27; Pittsfield Reply Brief at

5-6). Pittsfield also states that the record demonstrates that even under a higher capacity factor, the Termination Agreements still results in savings in accordance with the Department's standard of review (Pittsfield Brief at 28). Pittsfield asserts that a challenge by the Companies to the current Pittsfield operating procedures would only serve to reduce savings to ratepayers (id. at 25-27).

Pittsfield disagrees with the Attorney General that the Companies have an obligation to inform the Department of changes that occurred with respect to the 1992 PPAs after September 2003 or to "seek advisory opinion from the Department regarding prudent actions the Company might take on behalf of its customers" (Pittsfield Reply Brief at 4). Pittsfield maintains that the Attorney General cannot use the Department's decision in Tenaska to support his argument, because nothing in Tenaska imposes any obligation on the part of the Companies to bring disputes to the Department for resolution (id.). Pittsfield states that the major issue raised in Tenaska was whether the utility was required by the Department's then-current regulations to execute a "restated" PPA with a generator that had yet to construct its plant, in contrast to what Pittsfield characterizes as simply a matter of contract interpretation within the Department's jurisdiction (id.). Moreover, Pittsfield points out that Department recognized the advantages of a buyout over continued litigation costs in Tenaska (id. at 5).

Finally, Pittsfield disagrees with the Attorney General's argument that the dispute could have affected the value of the PPAs for other bidders in the auction process because of continuing uncertainty (id. at 6). Pittsfield states that the 2003 Auction was an open, competitive process (id.).

C. NSTAR Electric

NSTAR Electric states that the 2003 Auction was open and competitive and as such resulted in maximizing the mitigation of transition costs relating to the existing PPAs with Pittsfield (NSTAR Electric Brief at 6). The Companies claim that the Termination Agreements were the result of an open and competitive auction, consistent with (1) the Act's requirement to maximize the mitigation of transition costs, (2) the Companies' approved restructuring plans, and (3) Department precedent (id. at 3). The Companies maintain that they have demonstrated that the auction process ensured complete, uninhibited, non-discriminatory access to all data and information by any and all interested parties seeking to participate (id. at 6). The Companies assert that the auction produced multiple bidders and multiple types of bids, thereby allowing the Companies to analyze a number of options to determine which bid would maximize the mitigation of the transition costs associated with the PPAs (id. at 9).

The Companies argue that they properly considered all of the issues raised by the Attorney General on brief, and that entering into the Termination Agreements represents a reasonable settlement of the dispute that maximizes mitigation and customer savings (NSTAR Electric Reply Brief at 2). The Companies explain that they did, in fact, seek and receive a written opinion from their attorneys regarding the merits of the dispute (id. at 4). The Companies further explain that they reviewed the terms of the existing PPAs, conferred with counsel and had informal conversations with representatives of Pittsfield prior to sending Pittsfield the January 26, 2004 letter (id.). The Companies argue that they evaluated their legal position with no delay and, instead of jumping to costly and time-consuming litigation, they finalized negotiation of the

Termination Agreements taking into account all issues and providing for a resolution that maximizes mitigation of transition costs for customers (id. at 5).[8]

NSTAR Electric disagrees with the Attorney General's argument that it failed to pursue its contract rights under the existing PPAs and that this failure resulted in less than maximum mitigation of PPA costs (id. at 3). According to NSTAR Electric, after September 2003, which is when Pittsfield had altered the manner in which it dispatched its generating output into the power pool and thus reduced its capacity factor, NSTAR Electric's senior contract administrator had formal and informal contact with Pittsfield and NSTAR Electric's legal counsel regarding the merits of the dispute (id. at 4). Based on this contact, NSTAR Electric states that it considered pursuing the matter through formal litigation but believed that the cost to customers and the uncertainty of the outcome of formal litigation made negotiation of the buyouts a better resolution to maximize mitigation for customers (id. at 5-6). Therefore, NSTAR Electric argues that the Attorney General's assertion that NSTAR Electric did not explore all options with regard to the operation of the Pittsfield unit is incorrect (id. at 5).

NSTAR Electric states that the Termination Agreements will produce savings for customers even under the most conservative assumptions (NSTAR Electric Brief at 9). For example, NSTAR Electric claims that the Termination Agreements will result in customer savings even using historical (pre-September 2003) capacity factors of above 80 percent (up to 90 percent)

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[8] The Companies note that under Department regulations, qualifying facilities, and not distribution companies, have a regulatory right to petition the Department if they are aggrieved by actions of the distribution company (NSTAR Electric Reply Brief at 5, citing 220 C.M.R. § 8.08(2)).

as posited by the Attorney General (id. at 12). NSTAR Electric claims that the Attorney General incorrectly states that under a 90 percent capacity factor the savings are "very small," because such a high capacity factor of 90 percent is unreasonable and inconsistent with the historical capacity factor of the Pittsfield unit (id. at 11-12). NSTAR Electric states that assuming a 37 percent capacity factor for Pittsfield was a conservative assumption based on the actual capacity factor of the facility which has averaged approximately 27 percent over the past year (id. at 12). CEA also performed sensitivity analyses to determine the level of savings relating to the Termination Agreements under assumptions of both a ten percent increase and decrease in energy and fuel prices; there were significant savings under both scenarios (id. at 13). Finally, NSTAR Electric disagrees with the Attorney General's argument that the dispute regarding the operation of Pittsfield may have given an advantage to Pittsfield in relation to other potential bidders (NSTAR Electric Reply Brief at 8). NSTAR Electric states that it has demonstrated that the Pittsfield bid was the best viable bid received (id.). Moreover, NSTAR Electric argues that it is likely that if other bidders were fully informed about the decreased capacity factor and the likelihood of this trend in the future, any alternative bids would have been less favorable for customers (id.).

NSTAR Electric disagrees with the Attorney General's assertions that errors discovered in the filing's models raise questions regarding the accuracy of NSTAR Electric's and CEA's calculations (id.). NSTAR Electric admits that they corrected two faulty cells in the Excel spreadsheets used to compute the projected costs under the existing PPAs for Cambridge, and the correction increased the net savings for the Termination Agreements (id.). NSTAR Electric

asserts that the record contains corrected and reliable data which the Department can base its decision on, and no further verification is necessary or appropriate (id.).

Finally, NSTAR Electric proposes to change the timing of the payments between Cambridge and Commonwealth in 2005 and 2006 in order not to lose state tax benefits for the year 2005 (Exhs. NSTAR-1, Appendix A at 4; NSTAR-1 Appendix B at 4; NSTAR-GOL at 18; DTE-1-23; AG-3-14; RR-DTE-7). NSTAR Electric contends that it has demonstrated that these payment adjustments have the benefits of minimizing its tax obligation without affecting the total payments to Pittsfield (Exhs. NSTAR-1, Appendix A at 4; NSTAR-1, Appendix B at 4; NSTAR-GOL at 18; DTE-1-23; AG-3-14; RR-DTE-7).

NSTAR Electric states that its proposed ratemaking treatment for the costs of the Termination Agreements is consistent with Department precedent and should be approved (NSTAR Electric Brief at 14). NSTAR Electric requests to recover the over-market costs paid under the existing Pittsfield PPAs, and the cost incurred under the Termination Agreements through the variable portion of the Companies' respective transition charges (id. at 16). NSTAR Electric states that it also accounted for the fact that, through February 28, 2005, the electricity purchased through the existing PPAs is used to supply a portion of Cambridge's and Commonwealth's obligation to provide its customers with standard offer service (id. at 14).

VII. ANALYSIS AND FINDINGS

A. The Auction Process

In evaluating the divestiture of generation assets, the Department first reviews whether the divestiture process was equitable and structured to maximize the value of the assets being sold.

Western Massachusetts Electric Company, D.T.E. 00-68, at 12 (2000). In making these determinations, the Department considers whether the company used a "competitive auction or sale" that ensured "complete, uninhibited, non-discriminatory access to all data and information by any and all interested parties seeking to participate in such auction or sale." See G.L. c. 164, § 1A (b)(2). The Department has relied on the auction process also to determine whether a transaction involving a non-generation asset maximizes mitigation of transition costs. See Western Massachusetts Electric Company, D.T.E. 01-99, at 10 (1999); Cambridge Electric Light Company, D.T.E. 01-94, at 10 (1999).

The Department notes a number of features of the Companies' auction that highlight the competitive nature of the auction. First, a large number of parties participated in the Companies' auction; up to 90 parties were contacted initially, with 22 of those becoming Qualified Bidders, and 12 Qualified Bidders eventually submitting bids (Exh. NSTAR-RBH at 10-11, 17). Next, Qualified Bidders were provided with contract and invoice data on a uniform basis, and a formal mechanism was established to permit each Qualified Bidder to obtain additional information (id. at 9-15). Each Qualified Bidder was assigned a CEA representative who served as that bidder's single point of contact, allowing access to additional information while maintaining confidentiality (id. at 14). Qualified Bidders were free to submit bids on any combination of the Companies' 24 entitlements, in order to maximize the value of the portfolio (id. at 6; Exh. DTE-1-25).

The record demonstrates that the auction process ensured complete, uninhibited, non-discriminatory access to all data and information by all interested bidders and that the auction

process was competitive. Therefore, the Department finds that the auction process used was equitable and structured to maximize the value of the contracts sold.

With respect to the Attorney General's claim that the auction results were tainted by the dispute between the Companies and Pittsfield, the Department disagrees. First, there is no evidence that the Companies failed to properly value the PPAs. Historically, the Department has relied on responses from the market, such as bids selected from a properly structured auction process, as the relevant indicators of economic value. Where the Companies assigned a value to the PPAs, that value was used, with other data, to compare and screen bids for the purpose of ranking bids relative to one another; that ranking would remain unchanged regardless of the dollar value associated with a particular valuation. Second, there is no evidence to indicate any concern with respect to the management of or access to information in the auction process. Finally, there is no showing that the presence of the dispute affected this auction. While the Attorney General would assign an appreciable value to this dispute, there is no record evidence to indicate the dollar value that bidders placed on this dispute nor is there record evidence to indicate that the auction was not fair and competitive because of the dispute.

B. Maximization of Mitigation

The Attorney General argues that the Termination Agreements do not maximize the mitigation of the transition costs paid by the ratepayers because NSTAR Electric did not explore and pursue options other than the Termination Agreements that might have resulted in more savings (Attorney General Brief at 4-5). In particular, the Attorney General claims that the Companies failed to negotiate an even better termination agreement with Pittsfield, or simply

terminate the Pittsfield PPAs unilaterally based on Pittsfield's nonperformance (id. at 8).

The record demonstrates that the Companies did explore other options (Exhs. AG-1-1(u); AG-3-18; RR-AG-3). The Companies had conversations with and sent an official letter to Pittsfield after the dispatch of the plant changed (Exh. AG-1-1(u); RR-AG-3). On February 13, 2004, Pittsfield responded formally to the Companies stating that the way the unit was dispatched was consistent with the provisions of the PPAs and NEPOOL market rules (Exh. AG-1-1(v)). Because Pittsfield was reluctant to negotiate, NSTAR Electric considered pursuing the dispute through litigation, but, upon evaluation of its legal position, abandoned that plan (Tr. at 179; RR-AG-4).

The Attorney General questions the Companies' decision to enter into the Termination Agreements instead of pursuing other options relating to the existing PPAs with Pittsfield (Attorney General Brief at 5-9). There is no evidence in the record that pursuing this matter through litigation, even successfully, would have resulted in more savings to ratepayers than the savings achieved through the Termination Agreements. The record does not contain an estimate of the legal costs associated with the litigation; therefore, it is not possible to determine what the ratepayers final costs or savings would be if the dispute were pursued. In addition, even though there is an insufficient record to determine the probability that any of the options raised by the Attorney General were likely to be successful, it is clear from the record that Pittsfield was opposed to the other options, and customer savings would be less certain than under the Termination Agreements. Taking into account the level of uncertainty and expense associated with the suspension of the auction process and pursuing litigation of the dispute, in this particular

circumstance, the Department finds that the Companies' course of action in resolving the dispute by signing Termination Agreements with Pittsfield was reasonable. Therefore, the Department finds that the Companies took all reasonable steps to mitigate the ratepayers transition costs to the maximum extent possible. G.L. c. 164, § 1G.

Moreover, the Department finds that the dispute-related issues raised by the Attorney General on brief play little role in the determination of whether or not the Companies maximized mitigation of the costs for ratepayers, because the Department relies on the results of the auction to determine maximum mitigation. The Department has held, pursuant to the Act, that the results of a competitive auction are deemed to satisfy the requirement that the sale process maximize the value of the generation facilities being sold. D.T.E. 98-78/83, at 3-4, citing G.L. c. 164, § 1A(b)(1). An open, transparent, and fairly managed auction tests the market for, and the value of, an asset at the time of the offering. Id. at 10. The bid results of such a market test under proven fair conditions are strong evidence of an asset's worth. Id. at 10-11. Further, the Department has held that, under the Act, the bargained-for terms of a transaction achieved through "an open market-test is a better determinant of asset value than an administrative determination" and that "[o]nly upon the most compelling showing would the Department supplant the results of a market test." Boston Edison Company/Cambridge Electric Light Company, D.T.E. 98-119/126, at 29 (1999). When an auction process is used to divest of contractual entitlements, the marketplace has a chance to value the contracts and any above-market component should be treated in the same manner as other divestiture costs. See Id. at 33.

The Department has made its determination that the auction process provided complete, uninhibited, non-discriminatory access to all data and information by all interested bidders and that the auction process was competitive, and, therefore, structured to maximize the value of the PPAs. Therefore, the Department finds that the proposed Termination Agreements maximize the value of the PPAs and mitigation of the transition costs.

C. Customer Savings

NSTAR Electric claims that as a result of terminating the Pittsfield PPAs through the Termination Agreements, Cambridge's and Commonwealth's ratepayers will save approximately $7 million on a net present value basis in transition costs (Exhs. NSTAR-CAM-GOL-2 ERRATA at 1; NSTAR COM-GOL-2, at 1; Tr. at 13-14). In support of its claim, the Companies presented economic analysis of the future electricity market prices and the projected output of Pittsfield (Exh. RBH-6 CONFIDENTIAL).

The Attorney General claims that the number of errata that were necessary because of mistakes in the Companies' original filing raise doubts as to the accuracy of the models on which the Companies based their petition (Attorney General Brief at 10-11). For this reason, the Attorney General argues that the Department should not approve the Companies' petition until the calculations can be independently verified (id. at 11). The Attorney General's claim calls into question the quality of the Companies' information in the instant proceeding; however, the evidence provided by the Companies was subject to extensive discovery and cross-examination. In addition, the Companies provided electronic versions of documents that allowed for thorough examination by all parties of underlying formulas and calculations. For these reasons, the

Department finds that the number of errata in this proceeding do not rise to the level that would cause the Department to reject the record in this matter.

The Companies' calculations of customer savings are based on the Henwood forecast, which forecasts the future market price of electricity. The Henwood forecast is a widely-available and reasonable proxy for a forecast of the price of electricity. NSTAR Electric also ran its savings analysis under a variety of scenarios including various assumptions regarding the capacity factor of the Pittsfield unit and the market price of electricity; under all of these scenarios, the Termination Agreements still produce savings to ratepayers (Exh. DTE-1-33). After reviewing the Companies' economic analysis, the Department finds NSTAR Electric's claims of savings to be robust and credible under a wide range of assumptions, and that terminating the Pittsfield PPAs is likely to achieve savings to ratepayers.[9]

The Companies propose to recover the payments made pursuant to the Termination Agreements through the variable portion of the transition charge (Exh. NSTAR-GOL at 15-18). The Department finds that this proposal is consistent with the Companies' restructuring plan and

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[9] Due to tax timing issues, the payment stream to Pittsfield as described in the Termination Agreements is different for Cambridge and Commonwealth in 2005 and 2006 (Exhs. NSTAR-1, Appendix A at 4; NSTAR-1, Appendix B at 4). This payment stream results in higher costs to Cambridge ratepayers, but lower costs to Commonwealth ratepayers (Exh. AG-3-14; Tr. at 119-120). The net result of this cost shifting is a savings of approximately $100,000 for NSTAR Electric (Tr. at 119-120). Such subsidization of Commonwealth ratepayers by Cambridge ratepayers is contrary to Department ratemaking principles and precedent. See Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company, D.T.E. 03-121, at 47 (2004) (costs to serve one class of customer are to be recovered from those customers and not shifted to other customers). Therefore, the Department directs the Companies to include a true-up of this cost shifting from Commonwealth ratepayers to Cambridge ratepayers in the Companies' next reconciliation filing.

the requirements of the Act. Therefore, the Companies are permitted to recover the payments made pursuant to the Termination Agreements through the variable portion of the transition charge. However, the Department will reconcile all costs associated with the Termination Agreements in the Companies' future transition cost reconciliation filings.

Because terminating the Pittsfield PPAs is likely to achieve savings for ratepayers and because the savings mitigate NSTAR Electric's transition costs, the Department finds that the buyout is in the public interest and consistent with the requirements of G.L. c. 164, § 1G(d)(2)(ii). Therefore, the Department approves the Termination Agreements.

VIII. ORDER

Accordingly, after due notice, hearing, and consideration, it is

ORDERED: That the petition of Cambridge Electric Light Company and Commonwealth Electric Company for approval of the termination agreements entered into on June 2, 2004, by and between each of Cambridge Electric Light Company and Commonwealth Electric Company, and Pittsfield Generating Company, L.P., is hereby APPROVED; and it is

FURTHER ORDERED: That Cambridge Electric Light Company and Commonwealth Electric Company's proposed ratemaking treatment relating to the two termination agreements, is hereby APPROVED, subject to reconciliation and refund; and it is

FURTHER ORDERED: That Cambridge Electric Light Company and Commonwealth Electric Company comply with all directives contained herein.

By Order of the Department,

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Paul G. Afonso, Chairman

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W. Robert Keating, Commissioner

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Eugene J. Sullivan, Jr., Commissioner

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Deirdre K. Manning, Commissioner

Appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part.

Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such further time as the Commission may allow upon request filed prior to the expiration of twenty days after the date of service of said decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. (Sec. 5, Chapter 25, G.L. Ter. Ed., as most recently amended by Chapter 485 of the Acts of 1971).